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Approaching End of the European War

THIS Letter goes to press at a time when there is reason to hope that the end of the European war is only days, possibly only hours, away. Until very recently the opinion prevailed that the Nazis in the Alps and in other pockets would resist to a suicidal end. For their own evil purposes they had chosen to see their country wasted and destroyed, and no opposition group strong enough to take over and put a stop to the senseless slaughter had come forward. But those who expected a suicidal stand, and believed it would require a prolonged and costly campaign to overcome, may have taken insufficient account of the breathless speed of the dissolution of the German military, economic and political organization under Allied onslaughts, and of the effects of this disintegration on both the ability and the will to fight. When these are gone nothing is left but surrender. It may take place on the highest level of Nazi leadership, provided such leadership still is effective, or at various levels of the army command all the way down to the common soldier.

In the first case the end of the war on the scattered European fronts will be clear-cut; in the other the death throes may be drawn out, and it would be a mockery to proclaim the official V-E Day while our soldiers were still fighting and dying. At this writing there is no basis for firm comment, but the trend of events, official indications and the reports that fill the air all point to surrender by persons wielding the highest authority still existing in Germany, and consequently to a more clear-cut ending than earlier seemed possible.

Meanwhile the Japanese war will go on. The members of our forces on the Pacific front will do all that is expected of them, and more, and people at home must do no less.

Change in the Presidency

Events since the afternoon of April 12, when the news of the death of President Roosevelt fell with stunning effect upon the world, should inspire in all quarters a heightened sense of faith and pride in democratic institutions. Never before has the United States experienced a change in the Presidency during a war, and seldom in history have problems of such weight and scope been transferred from one man to another so suddenly and in so critical a time. But from every side has come a closing of the ranks. There has been grief and mourning, but not confusion, uncertainty or pause in the orderly functioning of government. President Truman has assumed his responsibilities with inspiring courage and confidence, and all parties and groups have vied in extending their support and in submerging their differences, so that the President may be free from the embarrassment of factional dispute in such a time.

Many people will see little to remark in either the orderly continuance of governmental processes or the manifestations of unity, since in this country nothing else was to be expected. But though we take these things for granted we should not pass them by as commonplace, for in vast areas of the world they do not exist. Nor do we enjoy them by virtue of accident or chance. Rather they express the strength of the democratic principles and institutions developed from the beginning of our history, and the power of those institutions to provide continuity of leadership in high office.

In the struggle in which we are engaged these principles and institutions, the devotion of people to them, and the ability of people to work together under them, are all being tested. On the battlefields and on the production lines the test has been met triumphantly. Unity has prevailed wherever and whenever unity was essential. Now the further test of a sudden change of leadership likewise has been surmounted. Not for a moment have our enemies been able to take comfort from the change. They have learned once more how enormous was their mistake in their failure to comprehend the fact that the American people in essentials are knit together in incomparable strength and solidarity.

The part that President Truman has played in this demonstration of unity has been deservedly acclaimed. His action in conferring promptly with members of both Houses of Congress and of both parties is significant of an intention to take counsel of Congress and work harmoniously with it in making the great decisions that are to come. In the cooperation and mutual respect of the executive and legislative branches, each within its own constitutional sphere, rests the highest hope of that balance in government which affords forward-looking leadership and effective administration, and at the same time both protects the liberties and expresses the will of the people.

General Business Conditions

Whether the official proclamation of V-E Day comes soon or late, the scale of hostilities will diminish, the requirements of the European front already are declining, and the adjustment from war on two fronts to war on one front is beginning. These are the facts of importance in the business situation. Economically, V-E Day becomes a period of time rather than a single day, and it is a period which has already begun.

During the past month most projects for construction of new war plants — for tanks, artillery and ammunition, high octane gasoline — have been cancelled. Schedules calling for increases in small arms ammunition and other important items have been suspended. Production of B-17 Flying Fortresses, B-24 Liberators and some other airplanes is being tapered off; and although a large part of the facilities released will be used for newer planes, the net effect will be a cutback. Announcement has been made that the huge Willow Run plant will be closed by August. Both merchant shipbuilding and naval construction are on the way down and will drop rapidly later in the year.

Against these cutbacks, requirements for some items are increasing. In certain items whose use is peculiar to the Pacific territory needs will be greater than heretofore, as troops are shifted from Europe. The Army Service Forces have stated that their overall requirements in the first quarter after V-E Day, although less than recent programs called for, will nevertheless be as great as in the first quarter of 1945. An earlier report that equipment now in Europe would be mostly left there and troops re-supplied for the Pacific has been authoritatively denied, with the statement that 70 per cent of Army equipment will be transferred. However, time will be required to recondition the material and concentrate it at European ports.

But even though the aggregate output of finished war goods may not decline greatly in the weeks just ahead, the downward trend is established and further cutbacks are to come. Meanwhile the forerunners of the change are being experienced by sub-contractors and materials suppliers, whose incoming orders naturally fall off earlier than finished goods production declines. The first to feel the effects of the cut in the airplane program are the manufacturers of engines and parts, and a significant sign of changing conditions is the War Manpower Commission's removal of the Detroit district from its list of areas of acute labor shortage (Group I). A number of other centers have been similarly reclassified. Another sign of the times is the easing in demand for copper and some other materials.

Factors in the Outlook

Business men recognize that these developments mark the beginning of a new phase in business, in which they will meet new conditions. The situation is a mixture of depressing and supporting factors, and the problem is to balance them out. Those who are inclined to hesitate stress the effects of cutbacks and the difficulties of shifting into civilian production the plants, labor and materials released from war use. At best, plants which have to reconvert will require periods ranging from a few days or weeks up to many months to get started again. The war still has first call, and facilities remaining for civilian work have to be parcelled out. The industrial organization is infinitely complex and interdependent, each industry relying for parts and materials on many others. Thus it is no good trying to make automobiles unless batteries, tires and upholstery fabrics, for example, can be had. Production is now balanced for war requirements. To restore the balance for peace requirements, and at the same time maintain the overall level, is a practical impossibility, and should be so recognized.

Meanwhile workers will be released, either to drop out of the labor force entirely, as many will do; to wait in idleness until reconversion is completed; or to move into other areas in search of work. Those who are displaced will suffer at least a temporary loss of purchasing power, and although they should have resources to carry them over, experience where cutbacks have been made shows that trade is affected. Outstanding commitments of retailers are heavy, and although both inventories and commitments are badly unbalanced and the need for many types of civilian goods is presently unlimited, nevertheless there may be hesitation.

There are other reasons for uncertainty, some of them fundamental. Determination of the principles and procedures for the sale of government surplus goods has been lamentably slow, and this concerns a good many lines.

Manufacturers are concerned over costs, in view of demands of workers for increases in hourly wage rates to maintain their take-home pay at the war levels as working hours are reduced, the danger of labor disturbances, and uncertainty as to productive efficiency. At the same time they do not know when they will be free of price controls or how restrictive ceiling prices will be under the controls. They have much reason for suspecting that there will be pressure on the profit margin from both the cost and price sides.

The Favorable Side

The foregoing represents one view of the situation. On the other hand, influences making for continued activity are present in extraordinary degree. There is no possible doubt that civilian requirements can absorb all the workers likely to be released from the war effort for some time to come, as fast as readjustment can be made, and that both deferred wants and spending power are stupendous. Looking ahead for any considerable period, this is the dominating factor in the outlook. People want immense quantities of clothing, new houses and equipment, automobiles and many other things. They have the money to buy them, and they will have still more purchasing power as they get work producing them. Industrial buyers want new machinery to make good deferred replacement and maintenance, and there are few if any manufacturing corporations which do not expect to make substantial capital expenditures, ranging up to the half billion dollar program of the General Motors Corporation and the billion dollar program of the American Telephone and Telegraph system. They will carry their programs forward in most cases as rapidly as possible, without regard for moderate business recession.

During the difficulties and readjustments of the transition period, the prospect of the demand waiting to be supplied should keep confidence strong and prevent a spiral downward. When business indexes turn down much depends upon whether the change is thought to be due to lasting or to temporary conditions. If business men think they can see the way through the valley, to a safe position on the other side, difficulties of the kind which now affect the short run are diminished by the widespread desire to get ahead and get a share of the business waiting to be done.

Moves Toward Reconversion

The immediate question is not how much work there is to do but how much can be done, — in short, how smooth will reconversion be. The War Production Board has moved rapidly during the month to facilitate preparations for reconversion. In anticipation of the day when resumption of automobile output can be permitted, it has authorized the automobile companies to place orders for $50,000,000 of tools under ratings which will put them directly behind urgent war orders, and the same ratings are available for manufacturers of high priority civilian goods generally. It has authorized expenditures by the industry of $35,000,000 on construction and $40,000,000 for rehabilitation of equipment. It has restored the "spot authorization" procedure — cancelled some months ago — under which firms whose war contracts are cut back or completed receive permission to resume production of civilian goods as the labor and materials supply permits.

The Board is also compiling new estimates of raw material requirements, the effect of which is virtually certain to make larger quantities of some materials available for civilian use in the third quarter. More steel than heretofore allotted has been definitely promised, and evidently more copper will become available. Mr. Krug, chairman of W.P.B., has reiterated the intention to rescind as early as possible as many as possible of the L and M orders restricting uses of materials, and has already made a start, although in the case of tin, natural rubber, lumber, textiles and certain chemicals controls will remain for an indefinite time.

At the same time the government agencies and services are pushing their pretermination program to facilitate settlement of cancelled contracts and clearance of plants, and have made desirable amendments in regulations. Mr. Byrnes in his report at the end of March said that 15,000,000 square feet of warehouse space to receive termination inventories and machines would be ready by June. The new tax proposals to speed payment of excess profits tax refund bonds and permit anticipation of loss carrybacks are moves to help corporations meet their need for working capital to cover reconversion expense. These moves all signify a strong consciousness of reconversion problems and of the governmental responsibility to facilitate their solution.

Questions of Policy

There are people in the country who sincerely believe that in the phase which the economic situation is now entering two types of action are greatly desirable, and as cutbacks increase much will be heard of their arguments. The first argument is that war production should be "tapered off," or maintained past the actual need, for the purpose of providing employment while industries are reconverting. Actually the Congress has considered this argument and refused to accept it, for in Section 202 of the War Mobilization and Reconversion Act of 1944 it is specifically provided

that war contracts shall not be continued "merely for the purpose of providing business or employment or for any other purposes other than the prosecution of the war." Of course, continuation of needless production wastes materials and labor and adds to the financial burden and the inflationary menace, which is an illusory way to seek prosperity. The claim that such a policy would cushion reconversion overlooks the fact that it would only defer unavoidable adjustments.

The second argument is that reconversion should be planned by overhead authorities, with government controls kept in operation for the purpose of guiding the process, for assuring that the most essential civilian requirements are supplied first, for providing equitable treatment for competitors, for looking after the interests of small business, or for other purposes considered economically and socially desirable.

One of the most searching discussions of these questions that has ever appeared is in in the third annual report of the Senate Special Committee Investigating the National Defense Program. This report was presented to the Senate March 3, 1944. The Committee was then headed by Senator Harry S. Truman of Missouri, now the President of the United States. Among many similar statements, it said:

> Some people favor attempting to formulate blueprints so as to regulate every step by which we attempt to reconvert from war to peacetime operations. They suggest that the Government should determine which manufacturers are to be permitted to make peacetime goods, what goods they are to be permitted to make, and even the terms and conditions under which they are to be permitted to sell the goods. It is argued that such decisions must be made by a Government agency in order to assure that the articles most needed are provided soonest by the manufacturers whose applications appear to have the greatest merit . . .
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> Decisions by Government may have to be made with respect to a few score complicated items that may be added to the list of essential civilian goods . . . However, the committee believes that to the extent that a surplus of material exists after provision has been made for war items and essential civilian items, manufacturers ought to be free to exercise their ingenuity in divising means of utilizing the surpluses for the production of any items they may choose.
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> Even in wartime, it was the flow of private initiative that made possible the success of the war program. This flow must be encouraged in the future. It is the job of Government to devise rules of the road, but not to tell the driver where he must travel . . .
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> As more and more materials become free in more and more different forms, articles which might possibly be made by combinations of the free articles will become both more numerous and more complex. This almost certainly will result in an intolerable burden upon any agency that may attempt to make the thousands of decisions that would have to be made if the Government is to attempt detailed regulation. In any event, it would place an intolerable burden upon the manufacturers, particularly the small and intermediate ones, for each manufacturer would have to come to Washington with hat in hand . . .
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> The greatest production and employment will be obtained by permitting those who are most energetic to obtain the materials that are surplus after allocations for war and essential items, providing (1) they do not pay prices above established ceilings and (2) they can establish, when questioned, that the materials purchased are intended for immediate use . . .
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> What the committee proposes in essence is that (1) we must not prevent the use of surplus commodities and thereby create unemployment, (2) we must not create a new series of unworkable industrial controls that will retard seriously the conversion from war production to the initial and most difficult stages of that conversion, and (3) we must not establish a pattern of regimentation for peacetime production, however good our intentions may be, because such regimentation will have a tendency to become permanent.
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> . . . If we unnaturally dam up and hold back production with controls that will be unworkable for mass operations, the difficulties and delays that will be incurred before such controls are discarded will cause great injury to industry and hardship to workers.

These are doctrines which can be echoed by every American citizen.

First Quarter Earnings

Corporate reports issued during the past month covering the first quarter show that although industrial activity as a whole was still maintained at near-capacity levels, the peak of war production has been passed and considerable irregularity has developed in the volume of sales as a result of cutting back many government contracts and at the same time expanding many others. Net income was stabilized, however, and the changes compared with last year were held within an unusually narrow range in most cases, by the high rates of corporate income and excise profits taxes which continue unchanged this year at 40 per cent and 95 per cent, respectively, with an 80 per cent overall ceiling. These taxes tend to offset to a major extent any increases or decreases in operating earnings.

A tabulation of the reports of 310 industrial companies shows that for the first quarter this year about 45 per cent of the companies had decreases in net income as compared with a year ago, while 55 per cent had increases. Combined net income (after taxes) of $332 million this year was 12 per cent below the $379 million reported in the fourth quarter of 1944, but 6 per cent above the $313 million in the first quarter of last year. Aggregate net worth of the group was $14,713 million at the beginning of this year, compared with $14,155 million at the beginning of last year, upon which the first quarter net income represented an annual rate of return of 9.0 per cent in 1945 and 8.8 per cent in 1944. The accompanying summary shows the changes by major industrial groups.

NET INCOME OF LEADING CORPORATIONS FOR THE FIRST QUARTER

Net Income is Shown after Depreciation, Interest, Taxes, and Other Charges and Reserves, but before Dividends—Net Worth Includes Book Value of Outstanding Preferred and Common Stock and Surplus Account at Beginning of Each Year.

(In Thousands of Dollars)

No. of Cos.	Industrial Groups	Net Income First Quarter 1944	Net Income First Quarter 1945	Per Cent Change	Net Worth January 1 1944	Net Worth January 1 1945	Annual Rate of Return % 1944	Annual Rate of Return % 1945
22	Food products	$ 19,744	$ 20,602	+ 4.3	$ 733,276	$ 739,297	10.8	11.1
13	Pulp and paper products	3.527	3,453	— 2.1	221,862	229,524	6.4	6.0
29	Chemicals, drugs, etc.	41.825	46,089	+10.2	1,568,960	1,663,866	10.7	11.1
14	Petroleum products	58.864	65,961	+12.1	2,813,183	2,951,574	8.4	8.9
13	Stone, clay and glass	7,934	7,273	— 8.3	359,020	368,520	8.8	7.9
26	Iron and steel	41,130	44,261	+ 7.6	3,362,086	3,397,858	4.9	5.2
8	Electrical equipment	17,925	18,215	+ 1.6	633,020	671,939	11.3	10.8
22	Machinery	8,106	7,180	—11.4	273,688	286,727	11.8	10.0
25	Autos and equipment	51,947	49,985	— 3.8	1,589,368	1,641,898	13.1	12.2
52	Other metal products	26,848	28,828	+ 7.4	1,110,514	1,186,006	9.7	9.7
33	Miscellaneous manufacturing	15,327	18,475	+20.5	474,136	514,373	12.9	14.4
257	Total manufacturing	293,177	310,322	+ 5.8	13,139,113	13,651,582	8.9	9.1
27	Mining and quarrying	12,236*	13,722*	+12.1	603,654	632,249	8.1	8.7
14	Trade (whol. and retail)	3.871	4,920	+27.1	245,243	261,418	6.3	7.5
12	Service and construction	3,646	3,167	—13.1	166,508	167,662	8.8	7.6
310	Total	$312,930	$332,131	+ 6.1	$14,154,518	$14,712,911	8.8	9.0

* Before depletion charges in some cases.

Among the more important industries that have reported, a group of 14 petroleum companies showed an increase over the first quarter last year in net income (after taxes) of 12 per cent, a group of 29 chemical and drug companies was up 10 per cent, and a group of 26 iron and steel companies was up 8 per cent, while a group of 25 automobile and parts companies was down 4 per cent.

Of 91 manufacturing companies reporting sales figures for the first quarter, those showing decreases as compared with a year ago outnumbered those showing increases by 5 to 3, and combined sales were down 4 per cent.

Europe's Reconstruction Problems

As the war in Europe reaches the mopping up stage, questions of economic conditions and prospects on the Continent, the status of life and property, and problems of reconstruction in general assume immediate importance. Compared with the situation at the end of the First World War, conditions at the end of this war will be in many respects far more difficult and problems far more serious. The economy of the Continent, regimented to serve the German war machine, has been turned from normal peacetime activity in unparallelled degree. Except in neutral countries, practically all areas have been overrun by battling armies at least once. Cities have been bombed and shelled into rubble. The destruction of buildings, means of communication, port installations, and industrial equipment has been on a scale never before comprehended. Dislocated, exhausted people, workers and refugees, numbering millions, are seeking rehabilitation.

The longer the war drags on the greater the loss and wastage of the resources that ought to be applied to reconstruction, and the greater the delay in freeing transportation and productive facilities for the work of restoration and the resumption of useful activities. That the destruction now is in large part of German property and resources, rather than those of her victims, is the justice of retribution, but there is little consolation in that fact for those whose problems are being augmented every day that the senseless struggle continues.

The problem of economic reconstruction fundamentally involves not only restoration of production and resumption of the exchange of goods, but adjustment to changes resulting from the war. To define it in terms of a return to prewar conditions is inadequate, because there can be no such return. The situation after the war will not be the same as before, either because of shifts in boundaries and resources, because of the steps that will be taken to make Germany militarily impotent, or because of changed political and social factors.

However, this broader readjustment is not the subject of first importance now, when the urgent problems are to produce and distribute food, to get railways and road transport in operation, to move displaced people where they belong, to provide housing, and to obtain the essential first supplies of material and equipment to enable the industries to start on the long road of recovery. The condition of the land, of the industrial plant, and of transportation are the basic factors.

In 1918 the war ended abruptly. There was enough railway equipment in most countries,

although it was over-age and in need of repair. Except in Northern France, Belgium, and part of Eastern Europe, where the industrial plant suffered from destruction, rehabilitation during the first year was primarily a problem of getting shipping space, of securing raw materials and foodstuffs, and of reconverting to peacetime production.

Now the presumption is that even when resistance on the Continent ends, war will go on in the Pacific. Continuation of controls over the use of shipping, raw materials, and foodstuffs is to be expected. An important part of the world, Southeastern Asia, with its wealth of raw materials and foodstuffs, will still be out of reach. Over all will be the immensely greater problems of rebuilding and repair.

Two conclusions may be drawn from the currently available information. First, reconstruction on the Continent of Europe is almost certain to be slower than after the First World War. Second, the pattern of reconstruction is likely to differ greatly from country to country. Not only are there different problems, different starting periods, and different physical conditions, but there are different governmental approaches and different political and social doctrines.

The Situation in Western Continental Europe

Although France and Belgium were overrun twice by the fighting armies, the destruction of productive facilities, according to available information, was relatively light, except where prolonged fighting took place or where the plants used by the Germans in their war effort were bombed. It is estimated that 75 per cent of French industrial capacity escaped undamaged, although in many cases equipment has suffered. A number of American-owned plants in both France and Belgium have been found in surprisingly good condition, ready to resume production when raw materials are available.

In contrast, the retreating Germans left the means of transportation in a bad state. In France, only a fraction of the pre-war number of locomotives was found in usable condition and of some 450,000 freight cars only 160,000 were left. Of 520,000 motor trucks less than 200,000 remained and most of those were laid up because of the lack of tires. The merchant marine tonnage dropped from 2,900,000 tons in 1938 to 850,000 tons. Most of the port installations were in ruins. The Belgian port of Antwerp escaped destruction but was set aside for military uses. The hard winter and lack of coal paralysed even the distribution of foodstuffs and raw materials available within each country.

The restoration of transport facilities thus became the number one reconstruction problem in both Belgium and France. It was attacked vigorously with the aid of army technicians. Considerable roadbed including bridges has been rebuilt and a number of French ports now handle record cargoes. Though the solution of the transportation problem is likely to be slow, both France and Belgium may be said to have turned the corner. Beginning this month, the French authorities will handle their own imports, except lend-lease shipments. With the shipping situation easier, access to the products of French Africa and Belgian Congo should be particularly helpful from the viewpoint of restoration of production. Much hope is also being placed in obtaining coal from the Saar and the Ruhr. Both countries have sufficient financial resources abroad to maintain a flow of raw materials and foodstuffs once the transportation and the fuel problems can be solved.

The situation in the Netherlands must enlist sympathy everywhere. The country derived its income from shipping, huge transit trade, highly developed agriculture, and from colonial investments. Now one-fifth of its valuable farm land, the greatest tangible resource left to the country, is reported flooded. Destruction is widespread, and starvation in the thickly settled occupied territory is appalling. The colonies are still to be wrested from the enemy, and the prospects for postwar transit business are poor in view of the collapse of Germany and the destruction of port facilities. The Netherlands has large external resources accumulated in the past, but the task of relief and rehabilitation will strain all the facilities that can be brought to bear upon it.

Unless Nazi resistance results in widespread destruction in Denmark and Norway, reconstruction in the two countries will pose problems of magnitude, but not of unique difficulty, except that rebuilding of livestock herds in Denmark will require time. In Norway, the urgent need is for food. The country has substantial funds abroad, which should help rebuild its merchant marine, the earnings of which normally pay for the bulk of its excess imports.

The purchasing power of the 45 million people of Italy has always been relatively low, and the devastation of war has been a shattering loss. Destruction of hydro-electric power installations not only affected railways, but crippled whatever industrial production remained. Progress has been made in rebuilding transportation facilities, but main reconstruction will have to wait until the industrial North, where damage has apparently been light, can provide new plant and equipment. Italy has hardly any funds to pay for imported raw materials to restart industrial production.

Germany Without Purchasing Power

Of all Continental countries, Germany will unquestionably be faced with the longest and thorniest road to reconstruction. Most of her industrial plant is virtually wiped out. If announced intentions are followed, Germany will be permanently deprived of some of her most valuable mineral resources in Upper Silesia and probably in the Saar. She may lose agricultural lands in the East which produced almost 30 per cent of her basic foodstuffs.

There will be reparation claims against Germany for goods stolen from her neighbors and for war damages. She may be stripped of some of her remaining equipment, and German manpower may be used, to aid reconstruction in the countries devastated by her armies. She will certainly be the last to obtain outside help.

The restoration of normal economic life will be further retarded by the necessity of military occupation, which may continue for a long time, especially if guerilla warfare or sabotage is attempted. Since each occupation zone will be governed independently, the extent of communication, transportation, and trade among the zones is doubtful. Most of the surplus food producing areas left to Germany will be in the Russian occupation zone, while the more industrialized districts will be occupied by the Western Allies. Military occupation may interfere also with the distribution of coal, around which the modern German industry has been built. It is said that as a result of war damage and dispersal of the miners, coal output may not be restored to even one-fourth of normal by Winter.

The impoverishment of the Germans is the effect of their own acts and, to the extent that it results from their senseless and fruitless resistance during the past months, of their own deliberate policy and choice. From the economic viewpoint, the question is, what are its consequences?

The Importance of Intra-European Trade

Germany was the third largest trading nation of the world before the war, accounting for almost 9 per cent of total international trade. Over 60 per cent of her peacetime trade was with other European countries and she was particularly important as a supplier of industrial goods and as a market for agricultural products of the great area of Central and Southeastern Europe stretching from Poland to Greece, and including over 110 million people or almost one-third of the Continent's population, excluding Russia. In 1937, she received over 20 per cent of total exports of the seven Danubian and Balkan countries and provided them with almost 25 per cent of their imports.

It is seldom realized how large and important intra-European trade has been. In the prewar years it was actually larger than the trade of Europe with the outside world, and considerably larger than the trade of non-European Continents with each other. The bulk of this trade was among the industrial countries of the Continent which exchanged with each other important raw materials and also various specialized manufactures.

The question now is, what will happen to this intra-European trade if it is not restored to its old channels, with industrialized Germany as the hub? For dependence of many European countries on German markets, in both directions, had been increased by the German bilateral trade policy of the 'thirties, and in the 'forties the conqueror had geared their economies into even closer relationship with its own.

What channels of trade will open up to supply Central and Southeastern Europe with the goods it needs and to absorb its own products? Will the answer be the industrialization of the agricultural countries, and if so by what means and with whose capital? How long will the readjustments take? What will be the repercussions in Europe and outside?

To pose these questions is to show how speculative any attempt to answer them would have to be, at this time. It is doubtful, in fact, if any overall plan formulated in advance can give the answer. Rather it is more likely that a series of partial solutions will be worked out. At first some communities will have to feed themselves and take care of their most urgent needs by cultivating the land and operating their local industries, patched up to the best of their ability. Then as they are able to produce a surplus of some goods they will find that other communities also have some surpluses which can be exchanged to advantage. The liberated peoples as a whole, according to the President's first report on UNRRA, will be able to supply over 90 per cent of the necessary food, clothing and other supplies.

Europe and World Trade

The final question concerns the relation of the European situation to the rest of the world. In considering that a prosperous Europe has depended upon trade among European countries themselves as well as with the outside world, there is also to be considered what a prosperous Europe has contributed to the prosperity of the world at large; and conversely, what the effects of a low standard of living in Europe for a prolonged time may be. Occupying only about 4 per cent of the total land area of the world, the Continent made its living literally as "the world's workshop". In the years immediately preceding World War II, it sold the rest of the world some $3¾ billion of goods annually, chiefly manufactured articles. In turn it bought almost $5 billion

worth of goods, mainly raw materials and foodstuffs. It absorbed almost 30 per cent of the total exports of non-European countries.

Of one thing we may be sure: Europe will be unable to export overseas on anything like the prewar scale until productive capacity is restored and both shipping and raw materials are available. Moreover, the need to rebuild and to supply dire shortages at home will occupy most of the producing capacity which normally would be devoted to export even though only the most pressing internal requirements will be accorded priority over foreign exchange-producing orders.

Europe's imports, with the vast accumulated needs in all countries, will initially exceed exports and will increase more rapidly, creating an abnormally large adverse trade balance which will have to be financed in part by drawing on gold and foreign exchange resources (substantial in several countries) and in part by the creation of credits. However, imports from overseas are likely to be limited for some time below prewar, in real values, both by reason of the necessity to conserve financial resources and because of limited supplies and transportation.

Import restrictions and rationing of foreign exchange will be relaxed only gradually. Imports of essential foodstuffs and of machinery and raw materials needed to restore production will have priority; and, in the case of most products, are likely to be limited by shortage of shipping and lack of surpluses in exporting countries, which have large accumulated internal demands of their own, rather than by lack of financial resources. The fact that available supplies of so many goods probably will be far less than enough to go around for at least several years after the war needs keeping in mind in connection with any program of foreign lending, since to expand buying power faster than goods would add to the inflationary danger.

The A.B.A. and Bretton Woods

"Why is the American Bankers Association opposing the Bretton Woods program?"

From the number of times this question is asked and the variety of answers given by critics of the A.B.A. position, it is evident that, despite all the talking and writing on the subject, there is still very little real understanding of what the argument is about.

With Treasury officials and other Bretton Woods advocates constantly preaching in public addresses, through the press, and over the radio that the Bretton Woods plan is indispensable to postwar currency stability and abandonment of discriminatory exchange practices, it is small wonder that people ask, "Why are the bankers opposed?"

The answer is that the bankers are *not* opposed, in the sense of being against what Bretton Woods stood for. They are just as much in favor of currency stability and elimination of discriminatory exchange practices as the Treasury or the delegates to the Conference. But being in favor of objectives is not enough. There must be a practicable plan. Too often in their zeal to "sell" the American people, the Bretton Woods enthusiasts have talked as though their particular plan offered practically a guarantee of postwar currency stability and freedom from exchange controls. Actually, of course, it does no such thing. No plan could; and certainly it needs but a casual glance through the extended and complicated provisions for *changing* exchange rates and *maintaining* exchange controls to see that Bretton Woods is no exception.

Yet such has been the force of propaganda that a large section of public opinion takes criticism having to do wholly with matters of method and technique as evidence of lack of sympathy with objectives. Not to go along with the official program in every particular has been to invite charges of ulterior motives, isolationism, and being a "reactionary".

Accusations Against "International Bankers"

There is, for example, the charge that bankers are opposing Bretton Woods because they want to make profits out of unstable exchanges. This follows an old familiar formula, based on appeal to popular prejudice and the fact that it is always possible to impress some people by attacking the bankers, especially the "international bankers of Wall Street".

Curiously enough, at the same time that bankers are being attacked by one group of critics for wanting to perpetuate unstable exchanges for selfish reasons, they are being accused by another group of seeking to drag an unwilling world back prematurely to the gold standard and rigid exchanges. Obviously, one of these accusations must be wrong; and it so happens that both are.

No group in the community has stood more consistently — even obstinately — for stable and orderly exchanges than the bankers. Bankers, almost to a man, opposed the departure from gold in 1933, and have overwhelmingly favored every approach to gold ever since. They were among the strongest advocates of repeal of the President's power to devalue the dollar. The fault, if any, in their attitude is that they have been too orthodox in their advocacy of the gold standard and fixed exchanges — which accounts for some of the criticism mentioned above, although anyone taking the trouble to read the A.B.A. report on Bretton Woods should be aware that the Association neither proposes or expects any general re-

turn to the gold standard in the near future. To charge now that bankers suddenly have become obstructionists to stabilization proposals for the sake of profits is to totally ignore this traditional viewpoint.

The fact is that bankers have very good and selfish reasons for *not* wanting fluctuating exchanges. The "profits" that can be made out of unstable exchanges are risky and speculative, and are quite as likely to turn out to be losses. Where banks make their surest and most money in exchange is in financing a large volume of foreign trade — a condition that thrives best under stable currencies. Mr. Edward E. Brown, president of the First National Bank of Chicago, member of the American delegation to Bretton Woods, and a warm supporter of the proposed International Monetary Fund, dealt effectively with the charge that banks want unstable exchange for profit when, in appearing before the House Banking and Currency Committee recently, he said:

> It is to the advantage of our bank to have exchanges that are stabilized, because the profits of our Foreign Exchange Department are based on the interest and exchanges that we get on handling foreign exchange transactions, and stable exchange promotes foreign trade and the more foreign trade there is, why, the more money we make. We do not make any speculative profit on our exchange position.

Nature of the Real Issues

In attempting to define the real issues posed by Bretton Woods, it might be useful to begin by stressing, for a change, the large area in which there is already agreement.

In the first place, there is — as stated above —already agreement upon objectives. The Association wants free and stable exchanges, and an international monetary organization to help achieve these conditions. Its record in this respect is clear and consistent. More than a year and a half ago, when the first Keynes and White currency stabilization proposals were under discussion, it said in a report by its Economic Policy Commission:

> Some international institution is desirable: to help nations in stabilizing their currencies; to provide a meeting place for the discussion of monetary questions; to collect information which is a necessary basis for sound decisions; and to make arrangements for stabilization credits in cases where they are justified.

That the Association is still in favor of these objectives is shown in its report on the Bretton Woods proposals issued on February 1 last, and in statements by Association representatives in hearings on the Bretton Woods Agreement Act before the House Banking and Currency Committee in March.

Secondly, the Association favors an important part of the particular machinery proposed at Bretton Woods for accomplishing these objectives. It endorses the International Bank for Reconstruction and Development as sound and desirable, and recommends its adoption with few changes.

Thus we come to the International Monetary Fund as embodying the main points of disagreement between the A.B.A. and the Treasury. What the A.B A. wants primarily is more assurance that the Fund will be operated as a stabilization fund should be — that is, concerned only with short-term credits required to iron out temporary irregularities in exchange fluctuations. It fears that the Fund, as proposed, is too elaborate and complicated, and by its system of quotas in an international money pool, managed by an international board, would make credit granting too easy and automatic, leading to bad loans, overborrowing, and postponement in countries experiencing exchange difficulties of those corrective internal measures necessary to insure real currency stability.

For such reasons the Bankers Association does not favor a separate International Monetary Fund, but recommends that certain proposed functions of the Fund be merged with the International Bank to be set up as soon as possible. Such an institution would be equipped to supply the kind of credit most needed in the reconstruction period, and such credits would be made selectively and after proper investigation. The United States in the case of the Bank would have a veto power over loans floated in dollars, just as other countries would have such power in respect to loans in their currencies.

The Bank, in the opinion of the A.B.A., could readily serve as the center for consultation and agreements between countries on currency matters, and provide stabilization credits where necessary and under proper safeguards. The Association believes that arrangements of this kind go as far as is practicable now in getting countries to really commit themselves as to currency policies and practices during the reconstruction period, and would be simpler, less costly, and more workable than the proposed Monetary Fund.

Treasury Opposition to A.B.A. Proposals

Treasury opposition to these proposals has been mainly on three counts:

1. That the Bretton Woods "agreement," having been "adopted" by 44 countries, cannot be changed without calling another conference.

2. That adequate safeguards against the misuse of the Fund feared by the A.B.A. are already embodied in the Articles of Agreement. Thus Treasury officials point out that, apart from quantitative limitations restricting (except upon special permission by the Fund) a member's net borrowing to a maximum of 100 per cent of its quota, with no more than

25 per cent in any one year, the Fund has authority both to postpone inauguration of exchange transactions with any member whose circumstances are such as might be considered likely to lead to improper use of the Fund, and to suspend exchange dealings at any time with a member deemed to be making improper use of the Fund. It is contended that these provisions refute the charge of easy and "automatic" lending, and were inserted with the purpose of insuring the same high standards of careful lending and liquidity emphasized in the A.B.A. proposals.

3. That merging the Fund with the Bank, in the manner proposed by the A.B.A., would "wreck the entire program" by doing away with the elaborately worked out formulas for dealing with changes in exchange rates and discriminatory exchange controls. As Mr. Dean Acheson, Assistant Secretary of State, recently put the argument:

> The heart of the Bretton Woods proposal is that there must be some action to get the nations to agree to abandon methods of economic warfare—such methods as competitive exchange depreciation, multiple currencies, and exchange controls.
>
> If you can't get countries to abandon these practices, it does no good to make stabilization loans.

Of these three objections, point number 2—is the lending sound?—must surely be considered of paramount importance. For without sound lending everything else goes by the board, regardless of how many nations may have signed or how solemn or sweeping their promises on currency policies and practices may be. Not only will the money of the lenders be frozen, but no favor will be done the borrowers who, instead of taking the basic steps necessary to correct their balance of payments, will be encouraged to go on borrowing and getting deeper and deeper in debt.

This suggests one of the several fallacies in the argument that because we spend hundreds of billions for war we can "afford" to risk $2¾ billion (U. S. subscription to the Fund) "for peace". It all depends upon the plan. While $2¾ billion might not be too much to pay for a good plan for international monetary stability, it would be a high price to pay for a bad plan.

If, as the Treasury insists, there is really agreement with the banking community on fundamental principles of how the Fund should operate, it ought not to be too difficult to find a means to express that agreement in ways that both parties can subscribe to, and which will be acceptable abroad as well. As now drawn, the Articles of Agreement contain so many obscurities and ambiguities of language on critical points that it is hard to tell what they really mean. Since the task of administering a fund of this kind will be a most formidable one at best, the management will have need of the clearest possible mandate as to what principles should govern.

A Suggestion by the C.E.D.

As a move in the direction of greater clarity may be cited the recent suggestion by the Committee for Economic Development that the proposed International Bank be given express authority to make stabilization and general purpose loans in cases where they are justified. Foreseeing the same danger envisioned by the A.B.A., viz., that the Fund—particularly in the postwar transition period—may become involved in loans which are of essentially long-term stabilization character, the Committee has proposed that the phrase in the provision of the Bank Agreement that "loans made or guaranteed by the Bank shall, *except in special circumstances* (italics ours), be for specific projects of reconstruction and development" be interpreted as definitely authorizing loans of the character just indicated. While it is true that the Bank managers might so construe the present language, if they chose to do so, the suggestion of the C.E.D. has the merit of making the language perfectly clear and removing all possible doubt as to what the powers may be.

The fact that the Treasury has indicated a receptive attitude towards the C.E.D.'s suggestion is encouraging evidence of recognition that the Bretton Woods document can still be changed to advantage, notwithstanding the much harped-on "agreement by 44 nations". The suggestion itself is good so far as it goes, but does not go far enough. While it opens up the Bank for a type of stabilization loan that belongs there rather than in the Fund, it does not at the same time necessarily imply a tightening up of the operations of the Fund. There is still serious question as to the adequacy of safeguards provided to assure proper discrimination in granting Fund credits.

Will Other Countries Accept Changes?

The question of the willingness of other countries to accept changes in the Articles of Agreement is of course pertinent, and deserves comment.

The first thing to be said is a reminder that the Bretton Woods plan has not been agreed upon by 44 nations, as so often loosely stated, but represents merely a set of proposals which the Bretton Woods delegations agreed to submit to their respective governments for consideration. The delegations did not even recommend the adoption of the proposals; and, in addition to this general reservation, there were specific reservations on a number of points by several delegations. The governments themselves remain entirely uncommited.

The second point that needs bringing out is the evidence from comments abroad that other

countries are going to take a good long look, including all the fine print, before signing on the dotted line. While the Bank has found general acceptance abroad, the Fund has met with a good deal of criticism and demand for clarification.

The British Chancellor of the Exchequer has characterized it as "a difficult document, inevitably long and technical." "There are," he said, "some obscurities of language in it which have led to misunderstanding and must be clarified."

Two leading British trade organizations — the London Chamber of Commerce and the National Union of Manufacturers — have issued statements severely critical of the Fund, while the Federation of British Industries, though approving the "broad objectives and principles" of the plan, calls attention to various "defects" and asks for interpretation of certain obscurities (for example, the term "fundamental disequilibrium"). The Federation further proposes an interim trial period of perhaps four years before the Government definitely commits itself to a universal multilateral system.

The London Economist, one of Britain's leading financial weeklies, observes in its issue of December 2, "The Bank is less controversial than the Fund and more urgently needed. In the Final Act the two are tied together, but if the Bank could be untied and set up separately, great advantage would result."

The following is from an editorial in the London Times of September 25:

> . . . Legitimate anxiety has been expressed over the possibility of a divergence of interpretation and of consequent misunderstanding on what may be a matter of vital concern to this country; and, whether arrangements of the kind described are contemplated in the immediate future or not, Parliament will rightly desire to be assured that other prospective parties to the draft scheme share without reservation the view of its effect taken by the Chancellor of the Exchequer and Lord Keynes . . .
>
> . . . This country is most anxious to cooperate loyally in any international arrangement, but it can hardly afford to face the alternative of either appearing as a defaulter or running into insoluble difficulties and failing to counter mass unemployment caused by the development of a slump elsewhere. The credit facilities provided by the Fund are, as one correspondent showed, a wholly inadequate safeguard against this contingency; for any sudden depression in the United States — such as occurred in 1929 and, with even greater rapidity, in 1937 — would almost instantaneously lead to exhaustion of Britain's credit with the Fund. It would seem difficult for any Government which has accepted the prime responsibility of maintaining a high and stable level of employment in the future to ratify the Bretton Woods agreement without further clarification of this issue . . .

The London Times comment raises a key question which has bothered a good many people, namely, whether there has been any real "meeting of the minds" between British and Americans on postwar currency policies, or whether we have been using language to create an impression of agreement without the substance. The British want a plan which leaves them plenty of room for flexibility in dealing with their postwar currency problems; we want a plan which puts more emphasis upon stability and firmer commitments. In an attempt to reconcile these differing viewpoints there has been produced a document which has been taken to mean one thing on this side of the Atlantic and another thing on the other side. Thus we hear the plan spoken of in this country as giving us something of the assurance of stability usually associated with the gold standard; while in England Lord Keynes has spoken of it as "the opposite of the gold standard." The impression that is left is of a kind of double talk which, however well intended, may be hurtful of real international understanding in the end.

Why Not Another Conference?

It is, of course, desirable to arrive at an understanding with other countries on monetary problems, if we can, without calling another conference. But why — if we have to have it — should we dread another conference? We are having two conferences to deal with security proposals — Dumbarton Oaks and San Francisco; and maybe more. In the economic area, other conferences must be held and will be useful in learning each other's point of view. One such conference is essential before long to consider trade arrangements, because trade quotas, tariffs, export bounties, bilateral agreements and the like could completely defeat any program for monetary stabilization. As Assistant Secretary of State, W. L. Clayton, recently told the Congress in testifying on the reciprocal trade agreements program, the Bretton Woods monetary agreements and other plans "won't make sense" without action in the tariff field. Trade policies and monetary policies should logically be considered together.

While we want to do all possible to capitalize and build on the progress of international monetary cooperation already begun, a program as important and complicated as this calls for much more than mere formal inspection and approval by the Congress. We need to give it the same careful study that other countries are going to give it, to the end that we reach an agreement that appeals to public opinion in this and other countries as both fair and practicable, and to which people can give their continuing support.

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